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EX PARTE OR LATE FILED

October 30, 1996

Ex Parte

Mr. William F. Caton
Acting Secretary
1919 M Street N.W., Room 222
Federal Communications Commission
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

RE: Ex Parte CC Docket No. 96-45, Federal-State Joint Board on Universal Service

Dear Mr. Caton:

Today Mr. A. Varner and Mr. A. Lombardo, representing BellSouth met with Commissioner Julia Johnson, member of the Federal-State Joint Board to discuss BellSouth's position regarding the above-mentioned proceeding. The attached documents represent the basis for the presentation and discussion.

Two copies of this notice and the attached documents are being filed with the Secretary of the FCC, pursuant to Section 1.1206(a)(2) of the Commission's rules.

Sincerely,



Cynthia Cox

Attachments

cc: Commissioner Julia Johnson (w/o attachments)

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Example of How the USF Could Be Jurisdictionalized

• Total USF:	\$21B
• Federal USF:	\$15B
• LEC Contributions (No surcharge):	\$7.5B
• Net support received by LECs:	\$7.5B
• Amount available for rate reductions	\$7.5B

Target to existing interstate support first:

• Interstate CCL	\$3.7B
• DEM Weighting	\$0.3B
• Existing USF	\$0.7B
• Total Interstate Reductions	\$4.7B
• Amount of Intrastate Reductions	\$2.8B

Note: For illustrative purposes only

Example of How the USF Could Be Jurisdictionalized

• Total USF:	\$21B
• Federal USF:	\$15B
• LEC Contributions (w/end-user surcharge):	\$0.0B
• Net support received by LECs:	\$15B
• Amount available for rate reductions	\$15B
Target to existing interstate support first:	
• Interstate CCL	\$3.7B
• DEM Weighting	\$0.3B
• Existing USF	\$0.7B
• Total Interstate Reductions	\$4.7B
• Amount of Intrastate Reductions	\$10.3B

Note: For illustrative purposes only

Changes to Universal Service Proposal

- Several changes were made to BellSouth's proposal in order to reflect the FCC Interconnection Order and to be consistent with the new USTA position:
 - » Use of an end-user surcharge rather than simply assessing companies for contributions to the fund
 - » Include business lines in fund size calculations (will have minimal impact for large companies, but could have significant impact for small LECs)
 - » Base proposal on affordability benchmarks and then jurisdictionalize the federal support

Universal Service Support Should Be Based on Actual Costs

- Actual costs reflect the actual network used to provide universal service
- Incremental costs reflect a theoretical network that does not exist
- Actual book costs reflect all the variables that impact costs (e.g.- extra costs that arise from hurricanes)

The SLC Should Not Be Decreased

- Loop costs have not decreased on an embedded basis
- Recovery of loop costs is ongoing since new loop plant continues to be placed:
 - » Place plant in new subdivisions
 - » Replace/reinforce plant in established neighborhoods
- Decreasing the SLC would increase the USF (an uneconomic outcome)

Q&A on Why the Subscriber Line Charge Should Not Be Decreased

Q. Given that the subscriber line charge has been in place for years, hasn't the loop plant associated with it already been recovered?

A. No. Local exchange companies are constantly placing new plant to provision loops. New plant is placed to provide service not only to new subdivisions, but also to replace or reinforce plant in established neighborhoods. Oftentimes, older plant has maintenance problems and needs to be replaced to ensure customers get the high quality service they expect. It should also be remembered that regulators have generally prescribed long lives for depreciation purposes, and that plant placed even two decades ago is still not fully recovered.

Q. The subscriber line charge has been frozen at \$3.50 for several years. Aren't loop costs declining and shouldn't the SLC be reduced to account for this decline in loop costs?

A. There are several reasons why this thinking is totally off-base. To begin with, the subscriber line charge only recovers a portion of the loop costs assigned to the interstate jurisdiction. The carrier common line charge (CCL) recovers about 40% of the costs assigned to the interstate jurisdiction and it is subject to reductions associated with the productivity factor that is inherent in price regulation. The other fallacy is the belief that loop costs are declining. On an embedded basis, loop costs are still generally increasing. This occurs because of inflation and higher hourly wages. It is true that the incremental cost of long loops is less than it was a decade ago because fiber plant has become more economical than copper plant for those loops. However, the incremental cost of short loops has increased in recent years due to an increase in the price of copper plant. Overall, loop costs have generally increased in the last decade based on embedded ARMIS cost data filed with the FCC.

Q. Wouldn't local service be more affordable if the SLC were decreased?

A. Local service is already affordable for just about everyone. Some 94% of customers nationwide subscribe to local telephone service. Of the 6% who don't subscribe, some just don't want phone service and others have had problems paying or controlling their toll bills. Since the SLC has been frozen since 1989, it has decreased considerably in real terms (i.e. - after taking inflation into account).

Q. What would happen if the SLC were decreased?

A. Since the actual costs that are recovered by the SLC would not go away, either the universal service fund would have to be bigger, the interexchange carriers would need to pay more or the recovery of costs would have to be shifted to the states.

UNIVERSAL SERVICE FINAL ORDER SUMMARY

The California Public Utilities Commission issued its Final Decision today in its Universal Service Proceeding. The vote was 3 to 1 with Commissioner Neepor dissenting on grounds which he will state in a written addendum to the decision.

Comparison of Pacific Bell Proposal, Proposed Decision and Final Order

Issue	Pacific Bell Proposal	Proposed Decision	Final Decision
Average cost of Basic Telephone Service	\$26.81	\$18.38	\$20.30
Subsidy Fund Size - Statewide	\$1.7B	\$268M	\$352M
Subsidy Fund Size - Pacific Bell	\$1.3B	\$158M	\$305M
Pacific Bell Lines Subsidized	9.7M	2.3M	2.7M
Collection Mechanism	Net-Trans Carrier Surcharge 16%	End-User Surcharge 1.07%	End-User Surcharge 2.87%
Amount Available to rebalance against subsidizing services (difference from "Subsidy Fund Size - Pacific Bell" is due to change from Net-Trans to End User Surcharge mechanism)	\$511M	\$158M	\$305M
Implementation Date	3/1/96	1/1/97	2/1/97

Size of Fund The Commission established a statewide universal service fund totaling approximately \$352 million to support the high cost areas of the state. Of this amount approximately \$305 million will go to Pacific to subsidize our highest cost service areas.

Statewide Average Cost The Commission adopted the Cost Proxy Model with changes that result in a statewide average cost of \$20.30 for residential basic exchange service.

Universal Service Subsidy Benchmark In those areas where the average cost of providing basic service exceeds the \$20.30 cost benchmark, the CPUC will allow a carrier to recover from the universal service fund the difference between cost of providing basic service (as determined by the Model) and a carrier's effective basic service revenue per line. Pacific's basic service revenue per line has been calculated by the Commission to be \$15.76 (\$11.25 monthly flat rate service rate, plus the \$3.50 End User Common Line Charge, plus \$1.01 for the Carrier Common Line Charge revenue).

Therefore if the average cost to provide service in a given area that Pacific serves is \$50 a month per line, Pacific would be able to recover from the

fund \$34.24 per line, per month (the difference between the \$50 cost and our \$15.76 revenue figure).

It is important to note that in areas where the average cost of providing basic service is between the \$20.30 cost benchmark and the \$15.76 revenue per line figure, those lines would receive no subsidy from the universal service fund. The subsidy for these lines would continue implicitly in our rate structure.

Funding of Primary Lines Only The universal service fund will only subsidize 1 line per household in those areas eligible for subsidy. Carriers will not receive any subsidy for any additional lines customers may have in their households.

End User Surcharge The newly created universal service fund will be funded by a 2.87% All End User Surcharge paid by the customers of all carriers providing telephone service.

Rate Rebalancing Any carrier, like Pacific receiving net funds from the newly created universal service fund must reduce their rates dollar for dollar. This reduction initially will be accomplished by an across the board surcredit on all products and services offered by a carrier. Carriers can file applications explaining how they would like to handle the revenue reductions on a permanent basis.

Funding for Schools, Libraries and CBOs In addition to the universal service fund, the Commission has established a California Teleconnect Fund to reimburse qualified carriers for providing discounts to schools, libraries, community-based organizations, and municipal and county owned hospitals and health clinics. The California Teleconnect Fund will be funded once again by a 0.41% all end user surcharge paid by the customers of all carriers providing telephone service. The total size of the California Teleconnect Fund is estimated to be \$50 million per year.

Economic Depreciation Rates The Commission accepted Pacific's proposal to use economic depreciation lives when calculating the subsidy as opposed to the prescribed depreciation lives advocated by AT&T, MCI, and others.

Funding in a Resale Scenario The CPUC also accepted our recommendation that facilities-based providers providing basic service lines at a below-cost price to resellers should receive any applicable subsidy and not the reseller.

Implementation Date The implementation date for the creation of the two funds, their associated surcharges, the application of the surcredit, and the mailing of bill inserts is scheduled for February 1, 1997.